MOODY'S
INVESTORS SERVICE

Rating Action: Moody's takes action on the ratings of 15 UK banks and building societies

12 Nov 2019

London, 12 November 2019 -- Moody's Investors Service ("Moody's") today took rating actions on 15 UK banks and building societies. The action reflects Moody's view that the operating environment is likely to weaken, given deteriorating institutional capacity and commitment to fiscal discipline in the UK, together with a worsening economy. This follows the change in outlook on the UK sovereign debt rating to negative from stable, which the rating agency announced on 8 November 2019 (Moody's changes outlook on UK's rating to negative from stable, affirms Aa2 rating; https://www.moodys.com/research/--PR_396604).

For all the affected lenders, Moody's affirmed the baseline credit assessments (BCA) and all ratings and assessments. For eight banks and building societies the rating agency changed the outlook on the long-term deposit and senior unsecured debt rating (where applicable) to negative from stable, for two to stable from positive, and for one it changed the outlook to negative from positive, while for four banks and building societies the outlook remained unchanged: negative (one lender), stable (one), or positive (two). The ratings and outlooks of all other rated banks and building societies that are domiciled in the UK or in the Crown Dependencies are unaffected by today's rating action.

Please click on this link http://www.moodys.com/viewresearchdoc.aspx?docid=PBC_205156 for the List of Affected Credit Ratings. This list is an integral part of this Press Release and identifies each affected issuer.

RATINGS RATIONALE

Today's action on UK banks and building societies was triggered by Moody's view that (1) UK public institutions have weakened, as they have struggled to cope with the magnitude of policy challenges that they currently face, including those that relate to fiscal policy; and (2) the UK's economic and fiscal strength are likely to be weaker going forward, and more susceptible to shocks than previously assumed by the rating agency.

These risks, if materialised, are credit negative for banks; a weaker operating environment will be credit negative for UK lenders, affecting their asset quality and profitability.

In particular, the net interest margins of many UK lenders have been progressively eroded by a prolonged period of low interest rates; furthermore, and especially following the ring-fencing of large UK banks, the residential mortgage market has become increasingly competitive, further reducing the margins for banks. The impact of the compression in the net interest margins is greater for those lenders that are highly concentrated in the residential mortgage sectors such as the building societies, but also banks such as Santander UK plc and Clydesdale Bank PLC. Other lenders such as Lloyds Bank plc have been able to partly offset the negative pressure on the margins for residential mortgages thanks to the greater diversification of their earnings being also driven by consumer credit, which has higher risks but also higher returns, lending and provision of fee-based services to corporates, asset management, and/or insurance.

Following years of moderate economic growth and low unemployment, the cost of risk of UK banks is low in the European context; in the first nine months of 2019, the five largest UK banks, which have a 47% combined market share for loans in the country, reported an average 30 basis points annualised cost of risk, which is low. Furthermore, following years of restructuring, problem loans are low, at just 1.7% of gross loans for the five UK banks as of end-June 2019. From this low point, however, the agency expects the cost of risk to rise, albeit moderately, as economic growth slows further.

Moody's does not have any particular governance concern for the banks and building societies included in this action, and does not apply any corporate behaviour adjustments to them.

FACTORS THAT COULD LEAD TO AN UPGRADE / DOWNGRADE

Upgrades to the banks' ratings is unlikely; however, an affirmation of the UK's sovereign debt rating, and an unchanged operating environment in the UK, could lead to a return to a stable outlook for the long-term deposit and senior unsecured debt rating outlooks affected by today's action, or a reversal to positive outlook for those moved to stable from positive.

Conversely, a deterioration of the banks' operating environment in the UK could lead to a downgrade of the BCAs and ratings for those banks with a negative outlook on their long-term deposit and senior unsecured debt ratings. The downgrade of the UK sovereign debt ratings could also lead to a downgrade of the long-term deposit and senior unsecured debt ratings for Lloyds Bank plc, Nationwide Building Society, and Santander UK plc.

SPECIFIC ANALYTICAL FACTORS FOR THE AFFECTED BANKS

BARCLAYS BANK UK PLC

Moody's affirmed the BCA and all ratings and assessments of Barclays Bank UK PLC (Barclays Bank UK), reflecting (1) robust capitalisation, stable earnings from its retail and SME businesses, moderate asset risk as well as limited exposure to wholesale funding, resulting in a BCA of a3; (2) low loss-given-failure for depositors of Barclays Bank UK, resulting in a one-notch uplift from the BCA; and (3) a further one-notch of uplift given moderate probability of government support.

The affirmation of Barclays Bank UK's BCA also takes into account social risk considerations. The bank has incurred substantial provisions related to the mis-selling of payment protection insurance (PPI). Moody's expects PPI charges to gradually reduce to zero; nevertheless, as the bank continues to process the information requests that it received until the 29 August 2019 deadline for UK consumers to claim compensation, PPI-related charges could remain volatile until at least the end of 2020.

Moody's changed the outlook on Barclays Bank UK's long-term deposit ratings to negative from stable, reflecting a weakening operating environment in the UK.

CLYDESDALE BANK PLC

Moody's affirmed the BCA and all ratings and assessments of Clydesdale Bank PLC (Clydesdale Bank) and its holding company Virgin Money UK PLC (Virgin Money UK), reflecting (1) good capitalisation and the potential for revenue and cost synergies over the next three years, but also limited business diversification, execution risks from its merger, and weak profitability, resulting in a BCA of baa2; (2) low loss-given-failure for depositors and senior bondholders of Clydesdale Bank, resulting in a one-notch uplift from the BCA, and high loss-given-failure for the senior bondholders of the holding company Virgin Money UK, resulting in ratings one notch below the BCA; and (3) low probability of government support, which does not result in any uplift.

The affirmation of Clydesdale Bank's BCA also takes into account social risk considerations. The bank has incurred substantial provisions related to the mis-selling of payment protection insurance (PPI). Moody's expects PPI charges to gradually reduce to zero; nevertheless, as the bank continues to process the information requests that it received until the 29 August 2019 deadline for UK consumers to claim compensation, PPI-related charges could remain volatile until at least the end of 2020.

Moody's changed the outlook on Clydesdale Bank's long-term deposit ratings, and on Virgin Money UK's senior unsecured debt rating to stable from positive, because a weakening operating environment in the UK offsets the potential for a stronger financial profile following a successful execution of the integration with Virgin Money PLC, which transferred most of its assets and liabilities to Clydesdale Bank on 21 October 2019.

CLOSE BROTHERS LIMITED

Moody's affirmed the BCA and all ratings and assessments of Close Brothers Limited and its holding company Close Brothers Group plc (Close Brothers Group), reflecting (1) a solid track record over economic cycles, strong capital and leverage, strong profitability and short duration of assets, resulting in a BCA of a2; (2) very low loss-given-failure for depositors and senior bondholders of Close Brothers Limited, resulting in a two-notch uplift from the BCA, and high loss-given-failure for the senior bondholders of the holding company Close Brothers Group, resulting in ratings one-notch below the BCA; and (3) low probability of government support, which does not result in any uplift.

Moody's changed the outlook on Close Brothers Limited's long-term deposit ratings, and on Close Brothers Group's senior unsecured debt rating to negative from stable, reflecting a weakening operating environment in the UK.

COVENTRY BUILDING SOCIETY

Moody's affirmed the BCA and all ratings and assessments of Coventry Building Society (Coventry), reflecting (1) strong asset quality and a high risk-based capital ratio, but also lower-than-peer leverage ratio, as well as the society's historically high growth rate in mortgage lending, which is partly mitigated by a strong track record of conservative underwriting standards, resulting in a BCA of a3; (2) low loss-given-failure for depositors and senior bondholders, resulting in a one-notch uplift from the BCA; and (3) low probability of government support, which does not result in any uplift.

Moody's changed the outlook on Coventry's long-term deposit and senior unsecured debt ratings to negative from stable, reflecting a weakening operating environment in the UK and the agency's expectations of continued pressure on the society's profitability.

LEEDS BUILDING SOCIETY

Moody's affirmed the BCA and all ratings and assessments of Leeds Building Society (Leeds), reflecting (1) strong capitalisation and sound funding structure, but at the same time heightened credit risk stemming from the society's rapid expansion of its loan portfolio, which is not fully seasoned, resulting in a BCA of baa1; (2) low loss-given-failure for depositors and senior bondholders, which results in a one-notch uplift from the BCA; and (3) low probability of government support, which does not result in any uplift.

Moody's changed the outlook on Leeds' long-term deposit and senior unsecured debt ratings to negative from stable, reflecting a weakening operating environment in the UK and the agency's expectations of continued pressure on the society's profitability.

LLOYDS BANKING GROUP PLC

Moody's affirmed the BCA and all ratings and assessments of Lloyds Banking Group plc (LBG), reflecting (1) low asset risk, stable core earnings and strong current levels of capital, which are, however, more susceptible to deterioration in a stress scenario than that of most of its peers because of the group's exposures to unsecured consumer loans and buy-to-let mortgages, resulting in a BCA of a3; (2) moderate loss-given-failure for senior bondholders, which does not result in any uplift from the BCA, and high loss-given-failure for the subordinate bondholders, resulting in ratings one-notch below the BCA; and (3) low probability of government support, which does not result in any uplift, reflecting the loss-absorbing nature of the wholesale bonds issued by holding companies.

The affirmation of LBG's BCA also takes into account social risk considerations. The bank has incurred substantial provisions related to the mis-selling of payment protection insurance (PPI). Moody's expects PPI charges to gradually reduce to zero; nevertheless, as the bank continues to process the information requests that it received until the 29 August 2019 deadline for UK consumers to claim compensation, PPI-related charges could remain volatile until at least the end of 2020.

Moody's changed the outlook on LBG's senior unsecured debt to negative from stable, reflecting a weakening operating environment in the UK.

-- LLOYDS BANK PLC

Moody's also affirmed the BCA and all ratings and assessments of Lloyds Bank plc (Lloyds Bank), reflecting (1) low asset risk, stable core earnings and stable funding, as well as weak leverage and the rating agency's expectation that loan impairments will increase, resulting in a BCA of a3; (2) very low loss-given-failure for depositors and senior bondholders, resulting in a two-notch uplift from the BCA, and high loss-given-failure for the subordinate bondholders, resulting in ratings one-notch below the BCA; and (3) moderate probability of government support for depositors and senior unsecured debt, resulting in a further one-notch uplift.

The affirmation of Lloyds Bank's BCA also takes into account social risk considerations. The bank has incurred substantial provisions related to the mis-selling of payment protection insurance (PPI). Moody's expects PPI charges to gradually reduce to zero; nevertheless, as the bank continues to process the information requests that it received until the 29 August 2019 deadline for UK consumers to claim compensation, PPI-related charges could remain volatile until at least the end of 2020.

Moody's changed the outlook on Lloyds Bank's long-term deposit and senior unsecured debt ratings to negative from stable, reflecting (1) a weakening operating environment in the UK, and (2) a potentially more limited capacity of the UK government to support the bank in case of need, as indicated by the negative outlook on the UK's sovereign debt rating.

NATIONWIDE BUILDING SOCIETY

Moody's affirmed the BCA and all ratings and assessments of Nationwide Building Society (Nationwide), reflecting (1) a very low stock of problem loans, very high risk-weighted capital ratios, stable revenues, negative pressure on margins and concentration of revenue and risks in UK residential mortgages, resulting in a BCA of a3; (2) very low loss-given-failure for depositors and senior bondholders, resulting in a two-notch uplift from the BCA, and high loss-given-failure for the junior senior unsecured and subordinate bondholders, resulting in ratings one-notch below the BCA; and (3) moderate probability of government support only for depositors and senior unsecured debt, resulting in a further one-notch uplift.

Moody's maintained a negative outlook on Nationwide's long-term deposit and senior unsecured debt ratings, reflecting (1) a weakening operating environment in the UK; (2) margin erosion in the UK residential mortgage market; (3) the risk that the society issues less debt than envisaged under its current funding plan, resulting in lower protection for senior unsecured debt and deposits in the medium term, as already incorporated in the current negative outlook; and (4) a potentially more limited capacity of the UK government to support the bank in case of need, as indicated by the negative outlook on the UK's sovereign debt rating.

NOTTINGHAM BUILDING SOCIETY

Moody's affirmed the BCA and all ratings and assessments of Nottingham Building Society (Nottingham), reflecting (1) strong asset quality and capitalisation, weak profitability compared to peers, a solid and stable funding and liquidity profile, but also geographical concentration in the Midlands and untested ability to access wholesale debt market, resulting in a BCA of baa1; (2) moderate loss-given-failure assessment for depositors, which does not result in any uplift; and (3) low probability of government support, which also does not result in any uplift.

Moody's changed the outlook on Nottingham's long-term deposit ratings to negative from stable, reflecting a weakening operating environment in the UK, and the agency's expectations of continued pressure on the society's net interest margin and profitability, exacerbated by its limited scale, which places Nottingham at a competitive disadvantage.

PRINCIPALITY BUILDING SOCIETY

Moody's affirmed the BCA and all ratings and assessments of Principality Building Society (Principality), reflecting (1) progress in reducing its legacy loan portfolio, thus improving its asset risk profile, which partially mitigates continued profitability pressures, as well as the society's strong capitalisation, and on the other hand, geographical concentration in Wales, resulting in a BCA of baa2; (2) moderate loss-given-failure assessment for depositors and senior bondholders, which does not result in any uplift; and (3) low probability of government support, which also does not result in any uplift.

Moody's maintained a stable outlook on Principality's long-term deposit and senior unsecured debt ratings reflecting the agency's expectation that the society will continue to reduce its legacy book while maintaining its strong capitalisation and solid funding profile.

THE ROYAL BANK OF SCOTLAND GROUP PLC

Moody's affirmed all ratings of The Royal Bank of Scotland Group plc (RBSG), reflecting (1) its high levels of capitalisation, solid retail and commercial bank earnings despite net interest margin and conduct cost pressures, as well as good levels of liquidity resulting in a BCA of baa2; (2) moderate loss-given-failure for its senior unsecured creditors, resulting in no uplift to the senior unsecured debt rating; and (3) low probability of government support, which does not result in any uplift to the senior ratings.

The affirmation of RBSG's BCA also takes into account environmental risk considerations. RBSG is exposed to some high-carbon emission sectors, which are prone to environmental risks. In 2018 power and oil and gas amounted to 1.2% of the group's lending exposures. However, RBSG's exposures are well-diversified geographically and on a single name basis. The BCA also incorporates social risk considerations. The bank has incurred substantial provisions related to the mis-selling of payment protection insurance (PPI). Moody's expects PPI charges to gradually reduce to zero; nevertheless, as the bank continues to process the information requests that it received until the 29 August 2019 deadline for UK consumers to claim compensation, PPI-related charges could remain volatile until at least the end of 2020.

Moody's maintained a positive outlook on RBSG's long-term senior unsecured debt ratings. Moody's believes that the group continues to make progress in restructuring, with this likely to be largely completed by the end of 2020.

-- NATIONAL WESTMINSTER BANK PLC

Moody's affirmed the BCA and all ratings and assessments of National Westminster Bank plc (NWB), The Royal Bank of Scotland plc (RBS), and Ulster Bank Limited (UBL), reflecting (1) moderate asset risk, good and stable profits from the retail and business banking activities, high capitalisation, high level of deposit funding and good levels of liquidity, resulting in a BCA of baa1; (2) very low loss-given-failure for its depositors, resulting in a two-notch uplift from the BCA; and (3) a further one-notch of uplift given moderate probability of government support.

The affirmation of NWB's BCA also takes into account social risk considerations. The bank has incurred substantial provisions related to the mis-selling of payment protection insurance (PPI). Moody's expects PPI charges to gradually reduce to zero; nevertheless, as the bank continues to process the information requests that it received until the 29 August 2019 deadline for UK consumers to claim compensation, PPI-related charges could remain volatile until at least the end of 2020.

Moody's maintained a positive outlook on the NWB's, RBS's and UBL's long-term deposit and issuer ratings. Moody's believes that the group continues to make progress in restructuring, with this likely to be largely completed by the end of 2020.

SANTANDER UK PLC

Moody's affirmed the BCA and all ratings and assessments of Santander UK plc (Santander UK), non-ring-fenced bank Santander Financial Services plc, and their holding company Santander UK Group Holdings plc (Santander UK Group), reflecting (1) the group's low stock of problem loans, good risk-weighted capitalisation and low earnings, but also a weak leverage ratio and profitability under pressure, resulting in a BCA of a3; (2) very low loss-given-failure for depositors and senior bondholders of Santander UK, resulting in a two-notch uplift from the BCA, and high loss-given-failure for the senior bondholders of the holding company Santander UK Group, resulting in ratings one-notch below the BCA; and (3) moderate probability of government support for Santander UK's depositors and senior debt, resulting in a further one-notch uplift.

Moody's changed the outlook on Santander UK's long-term deposit and senior unsecured debt ratings, and on Santander UK Group's senior unsecured debt ratings to negative from positive, reflecting a weakening operating environment in the UK. For Santander UK's long-term deposit and senior unsecured debt, the outlook change also reflects a potentially more limited capacity of the UK government to support the bank in case of need, as indicated by the negative outlook on the UK's sovereign debt rating.

SKIPTON BUILDING SOCIETY

Moody's affirmed the BCA and all ratings and assessments of Skipton Building Society (Skipton), reflecting (1) a low stock of problem loans, strong capital and stable retail funding, but also margin pressure and structural dependence on the UK housing market, resulting in a BCA of baa1; (2) moderate loss-given-failure for depositors and senior bondholders; and (3) low probability of government support, which does not result in any uplift.

Moody's changed the outlook on Skipton's long-term deposit and senior unsecured debt ratings to stable from positive, because a weakening operating environment in the UK offsets the society's reduced asset risk.

YORKSHIRE BUILDING SOCIETY

Moody's affirmed the BCA and all ratings and assessments of Yorkshire Building Society (Yorkshire), reflecting (1) strong asset quality, lower-than-peer mortgage lending growth rate and limited exposure to buy-to-let lending, in addition to its solid capitalisation, resulting in a BCA of baa1; (2) low loss-given-failure for depositors and senior bondholders, resulting in a one-notch uplift from the BCA, and high loss-given-failure for the junior senior bondholders, resulting in ratings one-notch below the BCA; and (3) low probability of government support, which does not result in any uplift.

Moody's changed the outlook on Yorkshire' long-term deposit and senior unsecured debt ratings to negative from stable, reflecting a weakening operating environment in the UK, and the agency's expectations of continued net interest margin pressure.

PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Banks published in August 2018. Please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

REGULATORY DISCLOSURES

Please click on this link http://www.moodys.com/viewresearchdoc.aspx?docid=PBC_205156 for the List of Affected Credit Ratings. This list is an integral part of this Press Release and provides, for each of the credit ratings covered, Moody's disclosures on the following items:

• Person Approving the Credit Rating

For ratings issued on a program, series, category/class of debt or security this announcement provides certain regulatory disclosures in relation to each rating of a subsequently issued bond or note of the same series, category/class of debt, security or pursuant to a program for which the ratings are derived exclusively from existing ratings in accordance with Moody's rating practices. For ratings issued on a support provider, this announcement provides certain regulatory disclosures in relation to the credit rating action on the support provider and in relation to each particular credit rating action for securities that derive their credit ratings from the support provider's credit rating. For provisional ratings, this announcement provides certain regulatory disclosures in relation to the provisional rating assigned, and in relation to a definitive rating that may be assigned subsequent to the final issuance of the debt, in each case where the transaction structure and terms have not changed prior to the assignment of the definitive rating in a manner that would have affected the rating. For further information please see the ratings tab on the issuer/entity page for the respective issuer on www.moodys.com.

For any affected securities or rated entities receiving direct credit support from the primary entity(ies) of this credit rating action, and whose ratings may change as a result of this credit rating action, the associated regulatory disclosures will be those of the guarantor entity. Exceptions to this approach exist for the following disclosures, if applicable to jurisdiction: Ancillary Services, Disclosure to rated entity, Disclosure from rated entity.

Regulatory disclosures contained in this press release apply to the credit rating and, if applicable, the related rating outlook or rating review.

The below contact information is provided for information purposes only. Please see the ratings tab of the issuer page at www.moodys.com, for each of the ratings covered, Moody's disclosures on the lead rating analyst and the Moody's legal entity that has issued the ratings.

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